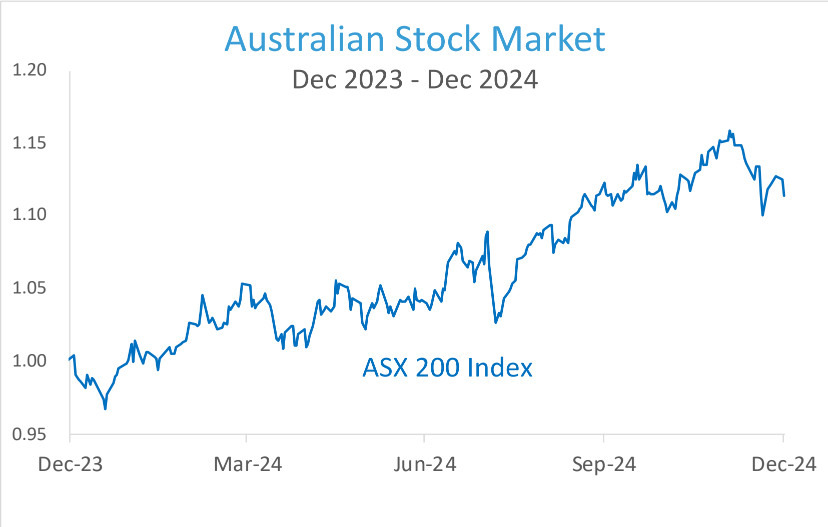
Financial Market Review for the December Quarter, 2024

In a year dominated by record stock market highs, geopolitical tensions, elections, and speculation around interest rates, the December quarter saw three cuts to the cash rate from the Federal Reserve and the election of Donald Trump, driving the US market to another dominant performance over other markets. But the December quarter finished with a holiday sell-down, providing a quiet end to a dramatic year.

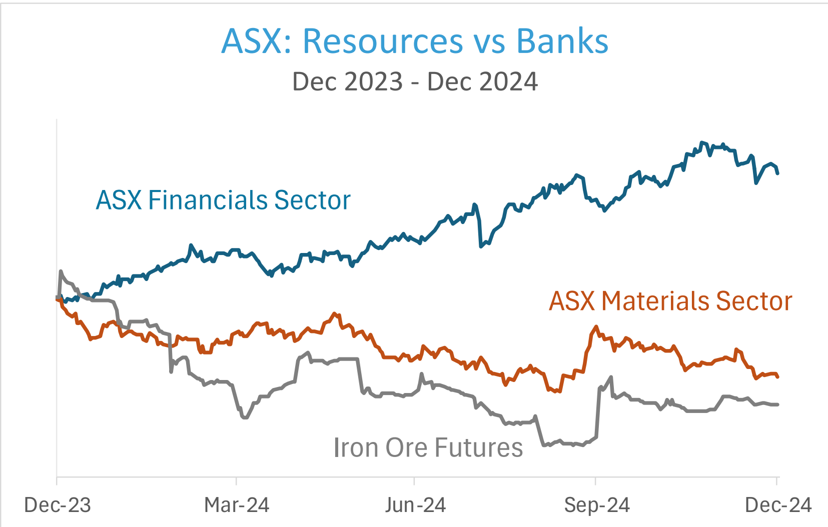
Financial markets have been on an unpredictable ride this year, driven by geopolitical tensions, from escalating tensions in the Middle East to Russia's war with Ukraine, China's economic wobbles, and Donald Trump's sweeping election victory. For the most part though, markets tended to ignore the global uncertainties and continued to move higher and higher.

A year ago, equity investors and strategists braced for a potentially turbulent 2024, worrying about the risk of a hard landing for the US economy and interest-rate cuts that could come too late to prevent it. Few anticipated that stock markets around the world would be hitting record highs by December.

The December quarter started in the same fashion, in what many were calling a "Santa Rally" in the lead up to Christmas – but it all came to an end in the last weeks of December when the Santa Rally turned into a Santa Sell Down.



The chart above shows the daily movement of the ASX 200 Index over the course of 2024. The market is up 11.4% for the year, but fell -3.3% in December alone, wiping out the gains made in October and November. It was a holiday slowdown come early, leaving the return for the quarter at just -0.8%.



The negative return in the quarter is mainly due to the poor performance of the Materials sector. Iron ore prices have tumbled by over 23% in 2024, due to concerns about weak demand from China's sluggish construction sector. Consequently, Australia's big mining stocks have returned double digit negative returns, and the ASX Materials sector is down by near -12% for the quarter and -13.7% for the year. Offsetting the poor performance of the miners has been the Financials Sector, the largest sector in the ASX 200 Index. The big banks returned 5.9% for the quarter and an impressive 33.7% for the year.

The ASX 200 was touching new highs right up to the 10th of December when the RBA had their final meeting of the year, leaving the cash rate unchanged at 4.35 per cent for the ninth consecutive time amid stubborn inflation and faltering economic growth.

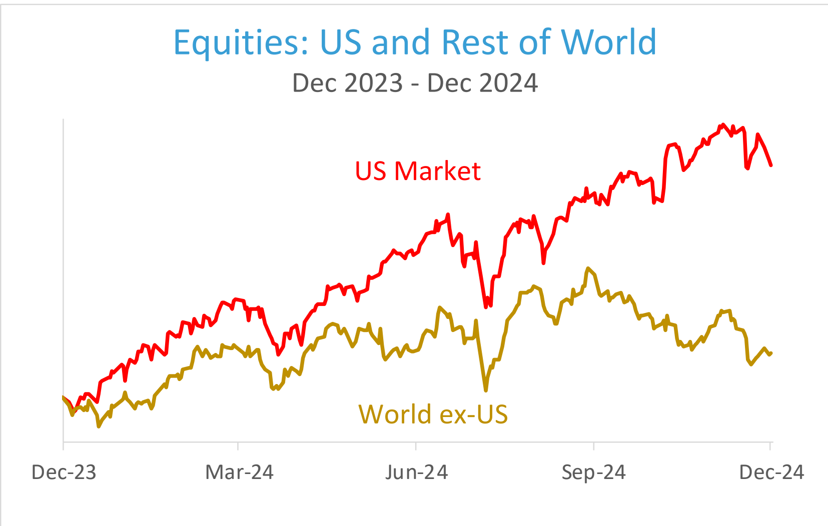
Just two days later Australia's unemployment rate unexpectedly dropped to 3.9%, one of the lowest in the world. Despite slow growth in the economy, the strong labour market had economists revise when Australia may get a rate cut, pushing the date back well into 2025. Waiting for the Australian cash rate to come down feels a bit like waiting for Godot to arrive…

On the other hand, the US has seen 3 rate cuts to boost along market sentiment. Starting with a 50bp cut in September, followed by 25bp cuts in November and again on December the 18th. These expected cuts, and the election of Donald Trump with policies that included further tax cuts and deregulation, saw a strong December rally with the S&P 500 Index projected to finish the year with a record high and one of the strongest annual gains on record.

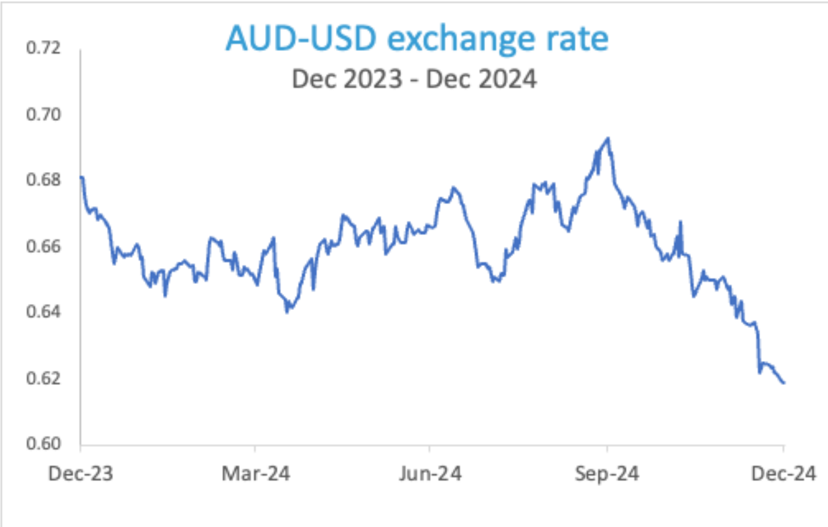
But the last rate cut December the 18th was accompanied by the Feds stating they will rein in the number of cuts expected in 2025 to two, signaling greater caution over how quickly borrowing costs can be reduced. The market also viewed Trump's tariff plans as potentially inflationary, negating the case for monetary easing and prolonging further rate cuts. Despite the interest rate cuts, longer term bond yields have been rising in expectation that inflation may remain high – or go even higher.

While the US stock market returned a remarkable 25% for the full year, between Christmas and New Year the S&P 500 fell by 2.6% while the tech heavy Nasdaq index fell by 3.5%. Overall, the index is up 2.4% for the quarter, but it was a quiet end to a dramatic year.

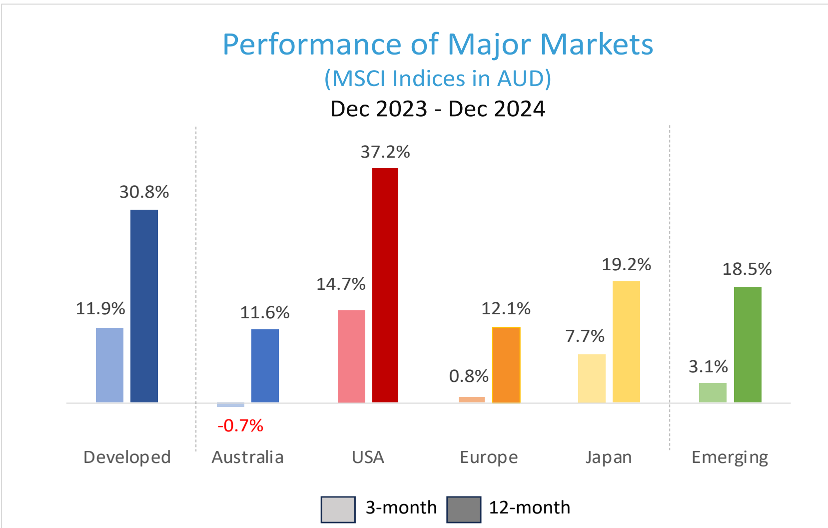
With rate cuts now reduced and prolonged, the US dollar rose to its highest level in 2 years. This can be seen when comparing the US to the rest of the world – in US dollar terms the World ex-US index returned -7.4% for the quarter and 4.7% for the year. The difference in returns of the US market and the rest of the world (in USD) one of the larges in nearly 30 years.



While the US Dollar appreciated against other developed markets, the Australian dollar ended the year below 62 US cents and down from 68 cents at the start of the year, as the weak domestic economy, concerns over China's outlook and a stronger US dollar took their toll. The Aussie is down -9.2% over the year, but all of that has come in the last quarter where the AUD has fallen by -10.7%.



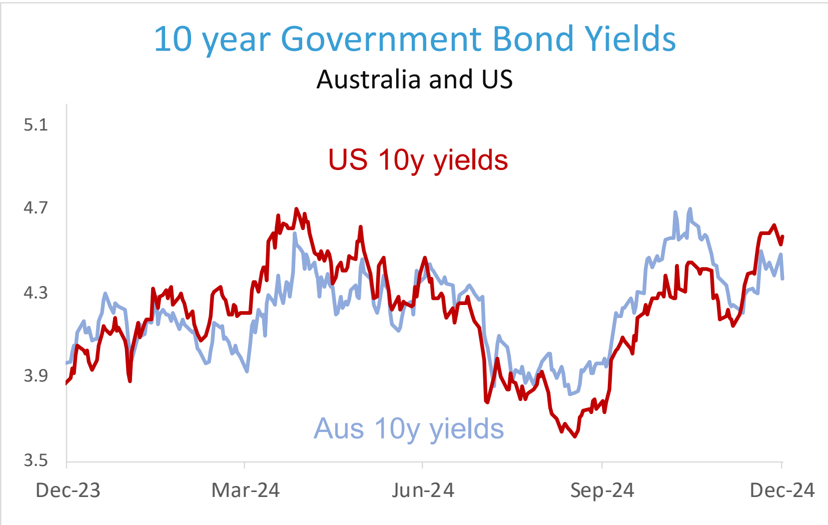
In Aussie dollar terms the rest of the world doesn't look that bad. In the chart below the US is the clear standout returning over 37% for the year (in AUD). Once again, the US market has been driven by a handful of mega cap tech stocks on the Nasdaq. The largest of these, Nvidia, is up 280% for the year. But other developed markets have had strong returns, with the broad MSCI World Index up over 30% for the year, and the Emerging Market index returning 18% for the full year.



Europe's economy continues to ride the edge between expansion and contraction, with expected growth around 1%, weighed down by the war in Ukraine, high energy prices and close ties to China's sluggish economy. In response, the European Central Bank (ECB) started cutting interest rates this year ahead of the US Federal Reserve (Fed), hoping to kickstart the eurozone economy.

In China, meanwhile, the government has launched a massive stimulus program designed to reverse chronic weakness in the country's real estate market and slowing industrial production. China's growth-oriented policies include interest rate cuts, mortgage rate reductions, and an aid package to help local governments deal with growing debt burdens. A cloud hangs over China's role in international trade as the incoming Trump administration has vowed to raise tariffs on Chinese imports.

While the changes in interest rates have been mostly been expected by the market, longer term bond yields have gone up, then down, up again and then down again… The December quarter has seen big rises in 10 year government bond yields in the US and Australia. Yields in the US and Australia are slightly up from where they were at the start of the year, so bond returns are fairly muted – returning less than cash for the year. But with 10 year yields around 4% there is plenty of room for bonds to provide protection in a balanced portfolio if equities do have a big correction.



Summing up, despite a holiday slowdown in the last weeks of December it's been an excellent 12 months in Australian and International equities. A diversified balanced portfolio has had another year of double digit returns. As 2024 has shown, forecasting what markets will do in the next 12 months is not an investment philosophy. The best approach is to stay disciplined in a diversified portfolio that has been designed to meet your long-term financial goals.

Dr Steve Garth
January 9th, 2025